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RUEHDK/AMEMBASSY DAKAR 2676
RUEHKM/AMEMBASSY KAMPALA 3094
RUEHNR/AMEMBASSY NAIROBI 5537
RUEAIIA/CIA WASHDC
RUEHGV/USMISSION GENEVA 2224
RHEHAAA/NSC WASHDC
RUEKJCS/JOINT STAFF WASHDC
RUEHC/DEPT OF LABOR WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
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C O N F I D E N T I A L SECTION 01 OF 03 HARARE 000545

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AF/S FOR B. WALCH
AF/EPS FOR ANN BREITER
NSC FOR SENIOR AFRICA DIRECTOR
STATE PASS TO USAID FOR L.DOBBINS AND J. HARMON
TREASURY FOR D. PETERS
COMMERCE FOR ROBERT TELCHIN
ADDIS ABABA FOR USAU
ADDIS ABABA FOR ACSS

E.O. 12958: DECL: 07/01/2019
TAGS: EFIN ECON PGOV ZI
SUBJECT: IMF BRIEFS ON GOZ PROGRESS, CONTINUING BUDGET GAP

REF: HARARE 232

Classified By: Ambassador James D. McGee for reason 1.4 (d)

¶1. (C) SUMMARY: During a June 29 briefing for OECD Ambassadors, IMF Mission Chief Vitaly Kramenko said his team found the GOZ budget evolving largely as expected, with revenues increasing steadily, but still inadequate to fully fund expenditures. He said the IMF is urging the GOZ to exercise caution on increasing wages. New legislation to improve Reserve Bank governance is before cabinet for action. The RBZ continues to operate without oversight, but with no revenue has to finance operations by selling assets. Finance Minister Biti explored with the IMF the possibility of a unilateral withdrawal of US$100 million of Zimbabwe's IMF quota to finance public investment. The IMF and the GOZ continue looking for ways that donor or IFI cash could close Zimbabwe's budget gap. END SUMMARY.

¶2. (U) On June 29 IMF Mission Chief Vitaly Kramenko briefed OECD Ambassadors on his team's one week follow-up to March 2009 Article IV consultations. Since March, IMF missions have also provided technical assistance on financial sector issues and revenue policy; a revenue administration team is due in July. Kramenko noted that this engagement was expensive and represented an unusual degree of commitment from the IMF.

Revenues up but still inadequate

¶3. (C) Kramenko said that, as expected, revenues have increased steadily since dollarization, from US$4 million in January to US$28 million in February, US$44 million in March,

US$53 million in April, US$65 million in May and US$70-80 million anticipated for June. Total revenues for the year were expected to reach US$850-880 million. Most of this is consumption based, originating in VAT and customs duties; corporate and income taxes are growing only slowly, as production remains low; the mining sector, for example, is only expected to produce about US$80 million this year. The IMF has recommended revenue policy reforms that would generate an additional US$50 million, bringing total tax receipts to US$930 million. South Africa (US$35 million) and China (US$5 million) have provided grants that will bring total revenue to US$970 million. With expenditures currently pegged at US$1.1 billion, Kramenko expressed the hope that pledges made to PM Tsvangirai during his recent trip to western capitals (totaling about US$220 million) would be sufficiently fungible to close the US$130 million budget gap

¶4. (C) The greatest threat to this relative balance, Kramenko said, comes from wage demands. Biti told the IMF that the GOZ wanted to increase the civil service allowance from
QGOZ wanted to increase the civil service allowance from
US$100 per month to US$150 per month, effective July 1. The IMF recommends that the GOZ phase in increases, paying US$112 in July, US$125 in October, and US$150 in CY 2010. Kramenko reported the Finance Ministry appears to support this cautious approach, but a political decision may be made instead.

Reserve Bank Reform Lagging

¶5. (C) Kramenko said that the Reserve Bank of Zimbabwe (RBZ) remains problematic. The financial sector team recommended a new governance structure for the RBZ and a division of the RBZ's abysmal balance sheet into a small entity with performing assets and a new vehicle to hold the RBZ's substantial hard currency liabilities, which would require some sort of financial resolution process. Kramenko said that draft legislation establishing a new RBZ Board and monetary policy committee has been submitted to cabinet. The IMF believes that contrary to advice, the GOZ will move forward legislation that would make the Governor chair of the Board, in line with practice in the region. Kramenko suggested that Gideon Gono's continuation as Governor and Board Chair was not critically important as long as the rest of the Board was made up of strong, independent members. The IMF team met with Gono for six hours. During the meeting, Gono assured the IMF that the RBZ and Ministry of Finance were working together amicably and that the RBZ supported reform. Kramenko noted that the current operations of the RBZ are completely opaque. The RBZ has no operating revenue, and is apparently selling assets to cover current costs. There are no financial statements and no outside body provides oversight.

Possible Unilateral SDR Withdrawal

¶6. (C) Kramenko said that Finance Minister Biti has expressed an interest in withdrawing some of Zimbabwe's quota of Special Drawing Rights (SDRs) to finance public investment and demonstrate the GOZ's ability to responsibly manage funds. Zimbabwe's quota of 353 million SDRs has a current value of more than US$540 million. Biti would like to withdraw US$100 million. Kramenko said that the IMF's Articles of Association gave the GOZ the incontestable right to make such a withdrawal -- no Board approval is required and existing arrears are not an issue. Following such a withdrawal, Zimbabwe would be required to pay interest at a market rate on the funds. Kramenko noted that such an action would go against the intent of the IMF system of quotas. He asked OECD Ambassadors what their governments would think of

such a withdrawal, implying that it might be acceptable to the international community. The OECD Ambassador group's reaction was surprise and dismay that such a possibility existed. Kramenko suggested that donors should tell Biti that negative reactions would far outweigh any positive demonstration effect if the GOZ undertook such an unusual step.

¶7. (C) Asked about next steps in Zimbabwe's engagement with the IMF, Kramenko said that technical assistance would Qthe IMF, Kramenko said that technical assistance would continue. The IMF will not consider adoption of a formal staff monitored program until and unless donors indicate commitment to bridge any financing gaps.

¶8. (C) COMMENT: The IMF remains focused on finding ways to help the Finance Ministry balance the books. With expenditures at a bare bones level and production slow, outside funding appears indispensable. We believe that the GOZ will find that recent donor pledges, like that of the USG, will produce only modest budgetary relief. We regret that Biti is considering a withdrawal of part of Zimbabwe's SDR allocation. Such a precedent could quickly result in a

complete exhaustion of Zimbabwe's quota -- and might encourage other developing countries to take similar unilateral action. END COMMENT.

MCGEE